JAPAN

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Key Economic Indicators

(Billions of U.S. Dollars unless otherwise noted)

	1996	1997	1998	
Income, Production and Employment:				
Nominal GDP	4,593.9	4,192.7	3,784.6	1/
Real GDP Growth (pct)	5.0	1.4	-2.6	2/
GDP by Sector:				
Agriculture	85.5	N/A	N/A	
Manufacturing	1,117.1	N/A	N/A	
Services	801.7	N/A	N/A	
Government	365.3	N/A	N/A	
Per Capita Income (US$)	30,014	N/A	N/A	
Labor Force (millions)	67.4	67.9	68.0	3/
Unemployment Rate (pct)	3.4	3.4	4.0	4/
Money and Prices (annual percentage growth):				
Money Supply (M2+CD)	3.3	3.1	4.0	3/
Consumer Price Inflation	0.1	1.8	0.8	3/
Exchange Rate (Yen/US$)	108.81	120.92	131.90	
Balance of Payments and Trade:				
Total Exports FOB	410.9	420.9	380.9	5/
Exports to U.S. FOB	111.9	117.1	116.8	5/
Total Imports CIF	349.1	338.7	278.7	5/
Imports from U.S. CIF	79.3	75.6	68.2	5/
Trade Balance	61.7	82.2	102.2	5/
Trade Balance with U.S.	32.6	41.5	48.6	5/
Current Account Surplus/GDP (pct)	1.4	2.3	N/A	
External Public Debt	0	0	0	
Debt Service Payments/GDP (pct)	0	0	0	
Fiscal Deficit/GDP (pct)	-4.4	-3.7	-3.4	6/
Gold and Foreign Exchange Reserves	217.9	220.8	212.1	7/
Aid from U.S.	0	0	0	
Aid from All Other Sources	0	0	0	

1/ January-June, seasonally adjusted, annualized.
2/ January-June, year-over-year, non-seasonally adjusted.
3/ January-August, non-seasonally adjusted average.
4/ January-August, seasonally-adjusted average.
5/ January-September, non-seasonally adjusted, annualized.
6/ Embassy projection.
7/ As of end-September 1998

Sources: Ministry of Finance; exports FOB, imports CIF customs basis; Economic Planning Agency; Bank of Japan, OECD Economic Outlook.

1. General Policy Framework

Japan's economy, the world's second largest at roughly 4.2 trillion dollars, is experiencing a significant recession, with most observers predicting a contraction of greater than two percent in 1998, following growth of only 1.4 percent in 1997.

Japan's current economic slowdown, which began in mid-1991, is the longest in its post-war history. (Until 1992-3, Japan had never experienced two consecutive years of less than 3 percent real growth in the postwar period.) A surge in asset prices to unsustainable levels and high rates of capital investment in the late 1980s gave way by 1991 to sharply slower growth, the need for corporate restructuring and balance sheet adjustment by businesses. A substantial fiscal contraction, which began in 1997, has dried up domestic demand. That, in addition to substantially weakened Asian demand for Japanese exports and banking system concerns, all continue to weigh heavily on the economy.

In recent years, the Japanese Government has used public spending to offset weak or negative private demand growth. Eight fiscal stimulus packages between August 1992 and April 1998 have boosted public investment spending substantially, while temporary tax cuts have supported public demand.

Japan's 1997 external accounts posted global trade and current account surpluses of $102 billion (BOP basis) and $94 billion, respectively. Through the first nine months of 1998, import volume shrank six percent due to negative domestic demand growth, while exports also declined by one percent. The current account surplus through the first nine months of 1998 grew by an annualized level of approximately $114 billion.

In order to ease credit conditions to support the economy, the Bank of Japan lowered the official discount rate nine times between mid-1991 and September 1995, from 6.0 percent per year to 0.5 percent. In September 1998, it guided the overnight call rate down further to 0.25 percent. The Bank of Japan also instituted some temporary programs to make credit more available to corporations.

2. Exchange Rate Policy

The yen has been volatile against the dollar in 1998. The average exchange rate through the first nine months of 1998 was 135 yen per dollar, versus 121 yen per dollar in 1997. A new Foreign Exchange Law in April 1998 significantly decontrolled most remaining barriers to cross-border capital transactions.

3. Structural Policies

Pricing Policy: Japan has a market economy, with prices generally set in accordance with supply and demand. However, with very high gross retail margins (needed to cover high fixed and personnel costs) and a complex distribution system, Japan's retail prices appear to exhibit a greater downward stickiness than in other large market economies. Moreover, some sectors such as construction are susceptible to cartel-like pricing arrangements, and in many key sectors heavily regulated by the government (i.e., transport and warehousing), it can still exert some limited temporary authority over pricing.

Tax Policy: Japanese corporate taxes are generally high by OECD standards. The government is committed to lowering the effective corporate tax rate from 47 percent to 40 percent within two years. Personal income tax levels vary by income bracket; the scale is highly progressive, but actual tax collection is below the OECD average. Temporary income tax cuts instituted for 1998 are expected to be made permanent in 1999, while the consumption tax was increased from three percent to five percent in April 1997.

Regulatory and Deregulation Policy: Japan's economy is highly regulated, but the government and business community recognize that deregulation is needed to spur growth. Still, opposition to change remains strong among vested-interest groups, and the economy remains burdened by numerous national and local government regulations, which have the effect of impeding market access by foreign firms. Official regulations also reinforce traditional Japanese business practices that restrict competition, help block new entrants (domestic or foreign) and raise costs. Examples of regulations that act as impediments include: prolonged approval processes for medical devices and pharmaceuticals; severe restrictions on foreign lawyers; the Japanese Government's tight regulation of all non-government employment services; and exceedingly high telecommunications interconnection rates.

In June 1997, the President and the Japanese Prime Minister agreed on an Enhanced Initiative on Deregulation and Competition Policy under the U.S.-Japan Framework Agreement. During its second year, the Initiative is focusing on achieving concrete deregulation in key sectoral and structural areas in Japan, such as telecommunications, housing, financial services, medical devices and pharmaceuticals, distribution, competition policy, and transparency in government rule-making. In April 1998, the Japanese Government issued a three year deregulation program which followed on the heels of its 1995 deregulation "Action Plan," which had been revised in 1996 and 1997.

4. Debt Management Policies

Japan is the world's largest net creditor. The Bank of Japan's foreign exchange reserves exceed $200 billion. It is an active participant together with the United States in international discussions of developing-country indebtedness issues in a variety of fora.

5. Significant Barriers to U.S. Exports

Japan is the United States' third largest export market, after Canada and Mexico. The United States is the largest market for Japanese exports. However, in many sectors U.S. exporters continue to enjoy incomplete access to the Japanese market. While Japan has reduced its formal tariff rates on most imports to relatively low levels, it has maintained nontariff barriers, such as non-transparency, discriminatory standards, and exclusionary business practices, and tolerates a business environment that protects established companies and restricts the free flow of competitive foreign goods into the Japanese market.

Transportation: In January 1998, the U.S. and Japan concluded a new agreement to significantly liberalize the trans-Pacific civil aviation market. This eliminated restrictions and resolved a dispute over the rights of longtime carriers to fly through Japan to other international destinations. It opened doors for carriers which recently entered the U.S.-Japan market, nearly tripling their access to Japan. The agreement also allowed code sharing (strategic alliances) between carriers for the first time, thereby greatly increasing their operational flexibility.

American carriers serving Japanese ports have long encountered a restrictive, inefficient and discriminatory system of port transportation services. After the Federal Maritime Commission (FMC) ruled in early 1997 that Japan maintained unfair shipping practices and proposed fines against Japanese ocean freight operators, the Japanese Government pledged to grant foreign carriers port transport licenses, and, at the same time, to reform the prior consultation system which allocates work on the waterfront and requires carriers to obtain approval for any change in their operations. The FMC imposed fines in September 1997 after Japan failed to carry out the reforms. Shortly afterwards, however, the government committed itself to actions that should, if fully implemented, provide a solid foundation for reform of Japanese port practices.

Agricultural and Wood Products: Some progress has been achieved through continued U.S. pressure on Japan to liberalize its markets for imported agricultural and wood products. However, tariffs on some processed food products remain relatively high, and other barriers to a liberalized market remain. For example, Japan continues to restrict, for phytosanitary reasons, the entry of numerous fruits and vegetables, such as pears and potatoes. In some cases, such as cherries, nectarines and apples, phytosanitary protocols may include only specific limited product varieties, excluding other, almost identical varieties. In accordance with its WTO obligations, Japan opened its rice market to imports under a Tariff Rate Quota (TRQ). However, the U.S. continues to press Japan to introduce this rice to consumers, rather than earmarking it for stockpiles or food aid to third countries. Tariffs for wood products are being reduced under Japan's Uruguay Round commitments, but they continue to pose barriers to market access. Moreover, a number of unresolved market access issues are being discussed in the U.S.-Japan deregulation dialogue, such as recognition of foreign testing organizations, approval of Japan Industrial Standards (JIS) grademark equivalency for U.S. manufacturers of nails, and Underwriters Laboratory's (UL) application for accreditation as a testing laboratory for fire materials.

Telecommunications and Broadcast: Japan is one of the 43 signatories of the Information Technology Agreement of 1997, which eliminates tariffs on the overwhelming majority of covered products by 2000. Access to telecommunications and broadcasting services remains constrained by both regulatory and monopolistic practices. In recent years, Japan has adopted a series of significant measures to foster a more pro-competitive regime in the telecommunications sector. However, barriers remain. New entrants face much higher costs and longer waiting period for connecting to the local dominant carrier's network than in other advanced countries, deterring competition.

There are foreign investment limits on cable TV and Direct-To-Home (DTH) satellite broadcasting companies. An unnecessarily burdensome regulatory system exists for DTH and telecommunications, impeding competitors' ability to operate in the most efficient way. Gaining access to utility and telephone poles and other facilities needed to build competing infrastructure is extremely difficult. Equipment testing and certification procedures are expensive and time-consuming. Foreign telecommunications equipment suppliers continue to have difficulty selling to the Japanese public sector, including NTT (Nippon Telegraph and Telephone), the largest purchaser of such equipment.

Standards, Testing, Labeling and Certification: Standards, testing, labeling and certification problems hamper market access in Japan. In some cases, advances in technology, products or processing make Japanese standards outdated and restrictive. Domestic industry often supports standards that are unique and restrict competition, although in some areas external pressure has brought about the simplification or harmonization of standards to comply with international practices. Fresh agricultural products continue to be subject to extensive restrictions, including phytosanitary restraints, required overseas production-site inspections, fumigation requirements and tariff rate or minimum access restrictions.

Japan requires repeated testing of established quarantine treatments each time a new variety of an already approved agricultural commodity is approved for importation into Japan. For example, Japan has approved red and golden delicious apples for importation, but required that the quarantine treatment be retested for other almost identical varieties. The U.S. challenged this redundant testing requirement in the WTO, arguing that it has no scientific basis and serves as a significant trade barrier. Completion of the testing for each variety takes at least two years and is costly to the U.S. Government and U.S. producers. In October 1998, a WTO dispute settlement panel found that Japan's varietal testing requirement for agricultural products violated its WTO obligations. Japan has appealed this decision.

Foreign Direct Investment (FDI): FDI in Japan has remained extremely small in scale relative to the size of the economy. In 1997, FDI totaled $6 billion, or 0.13 percent of GDP, as compared to $93 billion, or 1.5 percent in the United States. The low level of FDI reflects the high costs of doing business, the legacy of former investment restrictions, and a continuing environment of structural impediments to greater foreign investment. The challenges facing foreign investors seeking to establish or enhance a presence in Japan include: laws and regulations that directly or indirectly restrict the establishment of business facilities, close ties between government and industry, informal exclusive buyer-supplier networks and alliances, high taxation and opaque or incomplete accounting practices, and a difficult regulatory and opinion environment for foreign or domestic acquisitions of existing Japanese firms.

Recently, the Japanese Government has implemented potentially useful measures for increasing FDI, including easing restrictions on foreign capital entry. Still, most government investment promotion measures have been dictated by domestic priorities, and do not address the most important concerns of potential foreign investors. In addition, the acquisition of Japanese companies is difficult, due in part to crossholding of shares between allied companies and a resulting small publicly traded percentage of shares. This practice hinders the efforts of foreign firms wishing to acquire distribution or service networks through mergers or acquisitions.

In October 1998, the U.S. Government proposed to the Japanese Government 18 new reforms in the areas of mergers and acquisitions, land, and labor policy to improve Japan's environment for foreign direct investment.

Government Procurement Practices: Japan is a party to the 1996 WTO Government Procurement Agreement. While government procurement in Japan at the national, regional and local levels generally conform to the letter of the WTO agreement, there are reports that at some procuring entities, established domestic competitors continue to enjoy preferential access to tender information. In some sectors, unfair low pricing remains a problem, preventing companies from winning contracts based on open and transparent bidding procedures. Moreover, some entities continue to draw up tender specifications in a way that favors a preferred vendor, using design-based specifications rather than more neutral performance-based specifications.

Customs Procedures: The Japanese Customs Authority has made progress in automating its clearing procedures, and efforts are underway to integrate the procedures of other government agencies over the next several years. However, U.S. exporters still face relatively slow and burdensome processing.

6. Export Subsidies Policies

Approximately 16.8 percent of the $9.358 billion Japan allotted for official development in JFY 1997 was earmarked for loan aid (these figures do not include ODA for Eastern Europe or for 9 "graduated" countries). There are three categories of Japanese ODA: loan aid, grant aid, and technical cooperation. Japan has almost entirely eliminated tied aid credit in favor of loan aid (99 percent is untied, and the remainder is partially tied). However, there is suspicion that feasibility studies (funded by grant aid) to assist Asian countries may unfairly use Japanese-only specifications in the bidding process.

7. Protection of U.S. Intellectual Property Rights

Japan is a party to the Berne and Universal Copyright Conventions, the Paris Convention on Industrial Property, the Patent Cooperation Treaty, and the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs). Japan is on the Special 301 Watch List because of continuing U.S. concerns about the operation of Japan's patent system and the protection of trade secrets and computer software.

While Japan's IPR regime affords national treatment to U.S. entities, the U.S. has long been concerned by the long processing time for patent examination. Although Japan has recently cut patent pendency from 36 to 28 months, this is still longer than in other industrialized countries. Lengthy patent pendency, coupled with a practice of opening all patent applications to public inspection 18 months after filing, exposes applications to lengthy public scrutiny with the potential of limiting legal protection.

Many Japanese companies use the patent filing system as a tool of corporate strategy, making many applications to cover slight variations in technology. However, a February 1998 decision by Japan's Supreme Court to permit an infringement finding under the "the doctrine of equivalence" may reduce this practice and is a positive step toward broadening Japanese courts' generally narrow interpretation of patent rights. The rights of U.S. subscribers in Japan can be circumscribed by filings of applications for similar inventions or processes.

Japan's protection of trade secrets is inadequate. Because Japan's Constitution prohibits closed trials, the owner of a trade secret seeking redress for misappropriation of the secret is put in the difficult position of not being able to protect a trade secret without disclosing it publicly. While a recent amendment to Japan's Civil Procedures Act excludes Japanese court records containing trade secrets from public access, this legislation does not adequately address the problem. Court proceedings of trade secrets remain open to the public and neither the parties nor their attorneys have confidentiality obligations.

Japan's Trademark Law was revised in 1997 to speed the granting of trademark rights, strengthen protection to well-known trademarks, address problems related to unused trademarks, simplify registration procedures, and increase infringement penalties. The effect of the revisions, however, is not yet clear. Historically, trademark registration in Japan has been slow, requiring approximately 36 months. Since trademarks must be registered in Japan to ensure enforcement, delays make it difficult for foreign parties to enforce their marks.

End-user software piracy remains a major concern of U.S. and some Japanese software developers. An amendment to Japan's Civil Procedures Law to award punitive damages rather than actual damages would help increase the deterrent against software piracy.

8. Worker Rights

a. The Right of Association: Japan's Constitution and domestic labor law provide for the right of workers to freely associate in unions. Approximately 23 percent of Japan's labor force is unionized. The Japanese Trade Union Confederation (RENGO), which represents 7.8 million workers, is the largest labor organization. Both public and private sector workers may join a union, although members of the armed forces, police and firefighters may neither form unions nor strike. The right to strike, although implicit in the constitution, is seldom exercised. The law prohibits retribution against strikers and is effectively enforced.

b. The Right to Organize and Bargain Collectively: The constitution provides unions with the right to organize, bargain and act collectively. These rights are freely exercised, and collective bargaining is practiced widely, particularly during the annual "Spring Wage Offensive" of nationwide negotiations.

c. Prohibition of Forced or Compulsory Labor: Article 18 of the Japanese Constitution states that "No person shall be held in bondage of any kind. Involuntary servitude, except as punishment for crime, is prohibited." This provision applies both to adults and children, and there are no known cases of forced or bonded labor.

d. Minimum Age for Employment of Children: By law, children under the age of 15 may not be employed and those under age 18 may not work in dangerous or harmful jobs. Child labor is virtually non-existent in Japan, as societal values and the rigorous enforcement of the Labor Standards Law protect children from exploitation in the workplace.

e. Acceptable Conditions of Work: Minimum wages are set on both a sectoral and regional (prefectural) level. Minimum wages in Japanese fiscal year 1997 ranged from 5,368 yen ($44) per day in Tokyo to 4,625 yen ($38) in Okinawa. The Labor Standards Law provides for a 40-hour work week in most industries and mandates premium pay for hours worked beyond 40 hours in a week or eight hours in a day. However, labor unions criticize the Japanese Government for failing to enforce working hour regulations in smaller firms. The government effectively administers laws and regulations affecting workplace safety and health.

f. Worker Rights in Sectors with U.S. Investment: Labor regulations, working conditions and worker rights in sectors where U.S. capital is invested do not vary from those in other sectors of the economy.

Extent of U.S. Investment in Selected Industries -- U.S. Direct Investment Position Abroad on an Historical Cost Basis -- 1997

(Millions of U.S. Dollars)

Category		Amount
Petroleum		4,686
Total Manufacturing		14,293
Food & Kindred Products	408	
Chemicals & Allied Products	2732	
Primary & Fabricated Metals	349	
Industrial Machinery and Equipment	3885	
Electric & Electronic Equipment	2309	
Transportation Equipment	1744	
Other Manufacturing	2865	
Wholesale Trade		5628
Banking		565
Finance/Insurance/Real Estate		8839
Services		1177
Other Industries		380
TOTAL ALL INDUSTRIES		35,569

Source: U.S. Department of Commerce, Bureau of Economic Analysis.